No. ~~1328~~

IN THE

Supreme Court of the United States

OCTOBER TERM, 1966

SHELL OIL COMPANY,

Petitioner,

v.

PUBLIC SERVICE COMMISSION OF NEW YORK,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

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Shell Oil Company petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the District of Columbia Circuit entered on February 7, 1967.

Opinions Below

The opinion of the Court of Appeals is reported at — F. 2d —. The opinion and order of the Federal Power Commission (J.A. 277-309) are reported at 34 F.P.C. 897, and its opinion on rehearing (J.A. 315-321) at 34 F.P.C. 1330, for Texas Railroad Commission District No. 3 and at 34 F.P.C. 930 (J.A. 215-241) and its opinion on rehearing at 34 F.P.C. 1357 (J.A. 247-253) for Texas Railroad Commission District No. 2. The Commission's later opinions and orders, providing for refunds are not yet reported.

Jurisdiction

The judgment of the Court of Appeals reversing and remanding to the Commission for further proceedings was entered on February 7, 1967. This petition is timely filed and the jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1) and Section 19(b) of the Natural Gas Act, 15 U.S.C. 717r(b).

Statute Involved

The Natural Gas Act, June 21, 1938, c. 556, 52 Stat. 821-833, as amended, 15 U.S.C. 717-717w, provides in pertinent part as follows:

Section 7(c), 15 U.S.C. 717f(c):

> "No natural-gas company or person which will be a natural-gas company upon completion of any proposed construction or extension shall engage in the transportation or sale of natural gas, subject to the jurisdiction of the Commission, * * * unless there is in force with respect to such natural-gas company a certificate of public convenience and necessity issued by the Commission authorizing such acts or operations * * *. [T]he Commission shall set the matter for hearing and shall give reasonable notice of the hearing thereon to all interested persons as in its judgment may be necessary under rules and regulations to be prescribed by the Commission; and the application shall be decided in accordance with the procedure provided in subsection (e) of this section and such certificate shall be issued or denied accordingly: *Provided, however,* That the Commission may issue a temporary certificate in cases of emergency, to assure maintenance of adequate service or to serve particular customers, without notice or hearing, pending the determination of an application for a certificate * * *."

Section 7(e), 15 U.S.C. 717f(e):

> "* * * [A] certificate shall be issued to any qualified applicant therefor, authorizing the whole

or any part of the * * * sale * * * covered by the application, if it is found that the applicant is able and willing properly to do the acts and to perform the service proposed and to conform to the provisions of [the Act] and the requirements, rules, and regulations of the Commission thereunder, and that the proposed * * * sale, * * * to the extent authorized by the certificate, is or will be required by the present or future public convenience and necessity; otherwise such application shall be denied. The Commission shall have the power to attach to the issuance of the certificate and to the exercise of the rights granted thereunder such reasonable terms and conditions as the public convenience and necessity may require."

Question Presented

Does the Federal Power Commission have the power to consider "current conditions" in the industry, which include contract prices, intrastate market competition, and the effect of its own policies on those conditions, in determining the level of the "in-line" price, or is it restricted in its consideration only to those prices which it has previously permanently certificated, and which are no longer subject to review?

Statement

In the opinions and orders which were remanded by the Court of Appeals for the District of Columbia Circuit, the Federal Power Commission had determined the "in-line" price for two of the "pricing areas" in the Texas Gulf Coast, Texas Railroad Commission District No. 2, a ten county area in the vicinity of Corpus Christi, Texas, and Texas Railroad Commission District No. 3, a twenty-nine county area in the vicinity of Houston, Texas. For District No. 2, the Commission determined the "in-line" price to be 15¢ prior to September 28, 1960, and 16¢ per Mcf subsequent to that date (Opinion No. 476, 34 FPC 930).

For District No. 3, the Commission determined that the "in-line" price was 16¢ prior to September 28, 1960, and 17¢ per Mcf subsequent to that date. These determinations were based on a substantial record, which included studies of all contract prices in these areas since 1954, evidence of the competitive effect of the intrastate market, a particularly critical factor in this area because of the large and expanding local demand for natural gas for industrial purposes, and testimony by witnesses of the impact of the Statement of General Policy (18 C.F.R. § 2.56; 24 FPC 818) issued by the Commission on September 28, 1960, on gas prices in this area. Additional testimony on costs and economic conditions to support their contract prices was offered by the producers, but excluded by the Commission under its *Skelly* rule (28 FPC 401). This Court has sustained the Commission's discretion to exclude such evidence in a certificate proceeding under Section 7 of the Natural Gas Act in *United Gas Improvement Company* v. *Callery Properties, Inc.*, 382 U.S. 223, 15 L. ed. 2d 284, 86 S. Ct. 360.

The Public Service Commission of New York and certain gas distribution companies on the eastern seaboard[1] have long been engaged in a campaign to hold the gas prices in the Texas Gulf Coast Area to the lowest possible level. As a part of this campaign, these intervenors (so referred to because their status in the certificate proceedings before the Federal Power Commission is that of an intervenor in opposition to the producer-applicant) have selectively intervened in those certificate proceedings where the initial contract price level was above that level deemed "acceptable" by these intervenors. Under Commission procedure, the effect of these interventions was to require the trial of

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[1] Long Island Lighting Company, Brooklyn Union Gas Company and the Philadelphia Gas Works Division of United Gas Improvement Company.

these proceedings on a full record before a hearing examiner, with a review of the record and examiner's decision and briefs of the parties before the full Commission. This procedure is quite time-consuming, requiring three to five years to complete, or longer if accompanied by appeals to the Court of Appeals. Shell's dockets in these proceedings have been pending before either the Commission or the Courts since 1959. During all of this time, under the intervenors' theory, endorsed by the District of Columbia Circuit, the prices remain "suspect".[2]

There are a few sales of gas in these areas however, because of small quantities available, or extreme distances from existing pipeline systems, which cannot command the full market price.[3] The initial contract prices for these sales were therefore lower than the weighted average contract prices, and far below the highest contract prices, and also below the arbitrarily determined "acceptable" level of the intervenors. Because of the low level of these prices, no interventions were filed with the Commission against these sales, and therefore under the Commission's "shortened" procedure, permanent certificates were granted without opposition in a few months. These sales, say the intervenors, are the only sales which the Commission can look to to determine the price "line", because all other sales are "suspect" by virtue of the fact that they are being contested by these same intervenors on either the Commission or appellate Court levels.

The Commission properly rejected the limitation which the intervenors sought to place on their consideration of the price "line", finding that to do so would violate this Court's direction to keep the " 'in-line' price at the level where *substantial amounts* of gas have been certificated to enter the

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[2] *Public Service Commission of New York* v. *Federal Power Commission,* 329 F. 2d 242, cert. den. sub. nom. *Prado Oil & Gas Co.* v. *F.P.C.* 377 U.S. 963, 12 L. ed 2d 735, 84 S. Ct. 1644.

[3] Railroad District No. 3, 34 FPC 900, 901; (J.A. p. 281.) Railroad District No. 2, 34 FPC 936; (J.A. pp. 223, 224).

market under other *contemporaneous* certificates." (Emphasis supplied).[4] The Commission further found that to confine its consideration to previously-certificated, "non-suspect" prices, would merely operate to "freeze" the price "line", which would be inconsistent with the direction of the Ninth Circuit[5] and the Tenth Circuit[6] to change the "line" as necessary to give effect to "current conditions". The Commission also rejected producer contentions that the price "line" should be higher.

The intervenors appealed these Opinions to the District of Columbia Circuit (other appeals from other Commission decisions involving this question in other pricing areas were taken by both intervenors and producers to other Circuit Courts). That Court reversed the Commission's decision, finding that the Commission had committed reversible error in including in its consideration of factors making up the price "line", initial contract prices which had not been approved by the Commission, or which had been approved by the Commission through its procedure in issuing a temporary certificate under Section 7 of the Natural Gas Act. This Court has held that the powers of the Commission in issuing temporary certificates include powers to condition those certificates to protect the consumer in the "interim period" before rate regulation.[7] Nevertheless, the District of Columbia Circuit held that temporarily certificated prices would not be considered in determining the price "line."

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[4] *United Gas Improvement Company* v. *Callery Properties Inc.,* 382 U.S. 223, 15 L. ed 2d 284; 86 S. Ct. 360; at 15 L. ed 2d 288.

[5] *United Gas Improvement Company* v. *F.P.C.,* 283 F. 2d 817, (1960) cert. den. sub. nom. *Superior Oil Company* v. *United Gas Improvement Co.,* 365 U.S. 879, 6 L. ed 2d 191, 81 S. Ct. 1030; *State of California* v. *FPC,* 353 F. 2d 16 (1965).

[6] *Sohio Petroleum Company* v. *F.P.C.,* 298 F. 2d 465 (1961).

[7] *Federal Power Commission* v. *Hunt,* 376 U.S. 515; 11 L. ed 2d 878; 84 S. Ct. 861.

The D.C. Circuit admitted that the effect of its decision might be to cause a "freeze" of the "in-line" price. The Court said:[8]

> "It is true that our decision may cause the in-line price to be frozen temporarily during the interim period between sales of gas and the rate determination under § 4 or § 5 of the Act. This kind of freeze seems to be required by the logic of CATCO and in-line pricing."

Reasons for Granting the Writ

The decision of the Court of Appeals for the District of Columbia Circuit is in square conflict with the decision of the Court of Appeals for the Tenth Circuit in *Sunray DX Oil Company* v. *Federal Power Commission,* 370 F. 2d 181. Petitions for a writ of certiorari from that decision have been filed in this Court by the Brooklyn Union Gas Company, Long Island Lighting Company, Philadelphia Electric Company, and the Public Service Commission of New York, in Case No. 1135, on the same question presented here (Question No. 1) (the primary grounds alleged by petitioners there for granting the writ is the conflict with the D.C. Circuit's decision here sought to be reviewed). The Solicitor General on behalf of the Federal Power Commission has filed a Memorandum with the Court supporting that petition for certiorari on the grounds that a conflict exists between the two decisions of two Circuit Courts of Appeals, under Rule 19(b) of this Court. We therefore request that all of these petitions be consolidated for purposes of briefing and argument in this Court.

Subsequent to the *Sunray* case, the Court of Appeals for the Tenth Circuit has affirmed the Commission in *Pan American Petroleum Corporation* v. *Federal Power Com-*

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[8] — F. 2d —; page 25 of the slip opinion, attached hereto as Appendix A, pages 35, 36.

mission, — F. 2d —in which the Court found again that the Commission did not err in considering temporarily certificated prices in determining the price "line". The Tenth Circuit said:[9]

> "The general purpose of the Act is to protect the consumer, but section 7 proceedings, as well as other proceedings in the administration of the Act, must consider and attempt to obtain a balance between the interests of consumer, producer and all others whose interests fall between. The task is difficult, but experience has gradually attached more than lip-service significance to administrative expertise. Temporary certificates are now conditioned rather than perfunctorily granted. Contract prices have made some adjustment in view of the inescapable captured market of regulation."

The attachment of price conditions on permanent certificates has always been discretionary with the Commission, and the Commission decision in establishing a price "line" is based on its expertise and careful consideration of all factors. Unless it abused its discretion, the Commission's decision must be sustained.[10] This Court said in CATCO:[11]

> "Where the proposed price is not in keeping with the public interest because it is out of line or because its approval might result in a triggering of general price rises or an increase in the applicant's existing rates by reason of 'favored nation' clauses or otherwise, *the Commission in the exercise of its discretion might attach such conditions as it believes are necessary.*" (Emphasis supplied.)

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[9] Page 15 of the slip opinion. The case is not yet officially reported, so is attached as Appendix B hereto, for the convenience of the Court. (Quote appears at page 56 of Appendix B.)

[10] *Sunray DX Oil Company* v. *F.P.C.*, 370 F. 2d 181 at 190 (U.S.C.A. — 10th, 1966); *State of California* v. *F.P.C.*, 353 F. 2d 16 at 22, 23 (U.S.C.A. — 9th, 1965).

[11] *Atlantic Refining Company* v. *F.P.C.*, 360 U.S. 378; 3 L. ed 2d 1312; 79 S. Ct. 1246, at 360 U.S. 391.

The discretion of the Commission to look at factors other than its own permanently certificated prices in determining the price "line" is essential in the public interest. Otherwise there is no way that the Commission can compensate for changing "current conditions" by changing the price "line" accordingly, either up or down, except through a full-blown rate proceeding under Sections 4 and 5. This Court has held that this type of proceeding is not feasible in a proceeding under Section 7.[12]

Under the price "freeze" theory adopted by the District of Columbia Circuit, Section 7 of the Natural Gas Act is effectively written out of the Natural Gas Act, once the Commission has determined the "in-line" price for a given area. There is no way that the Commission can review, short of a full-blown rate hearing under Sections 4 and 5, the adequacy of supply in the area, and whether the price "line" established for the late 1950's is still in the public interest some ten years later. In *CATCO* this Court charged the Commission to insure that natural gas is sold ". . . at the lowest reasonable rate consistent with the *maintenance of adequate service* in the public interest" (360 U.S. at 388) (Emphasis supplied). The Commission determined in this case that the price "line" which it had fixed in the late 1950's was not sufficient to insure an adequate supply of gas for the interstate pipelines in the Texas Gulf Coast Area in the late 1960's. The District of Columbia Circuit Decision would require the Commission to "roll-back" prices to levels in effect ten years earlier, having "no current relevancy".[13]

The Decision Below has the practical effect of divesting the Federal Power Commission of jurisdiction to determine the price "line", a power granted to it by Congress under Section 7 of the Natural Gas Act, as interpreted by this Court in *Catco and Callery,* and vesting such jurisdiction

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12 *United Gas Improvement Co.* v. *Callery Properties Inc., supra.*

13 Such a roll-back was expressly rejected by the Ninth Circuit in *United Gas Improvement Co.* v. *F.P.C.,* 283 F. 2d 817 at 824.

in the Public Service Commision of New York [14] and the other intervenors. By the simple expedient of selecting the price level it deems acceptable, and intervening in all certificate proceedings where contract prices exceed that level, the New York Commission can make all prices not acceptable to it "suspect". Under the Decision Below the Commission is then precluded from considering these prices in its determination of the "line". In this way the New York Commission can, and has, if the Decision Below is not set aside, determined the "in-line" price for the pricing areas here in question.

The D. C. Circuit seeks to de-emphasize the impact of the "in-line" price "freeze" by noting that it is only effective until the Commission had determined a just and reasonable rate for the area in question. As the Court is aware, this "interim" for the Texas Gulf Coast Area is already thirteen years long, with the final decision in the Texas Gulf Coast Area Rate Proceeding (FPC Docket No. AR64-2) at least two years away. Moreover, the Commission has already determined that the just and reasonable rate which it determined in the Permian Area [15] will be the "in-line" price for that area.[16] Therefore the determination of a just and reasonable rate will only end one "interim" period and commence another. If it is to protect the public interest, the Commission must have the power to adjust this price for future contracts in the period between just and reasonable determinations under Sections 4 and 5 of the Natural Gas Act.

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[14] The Public Service Commission of New York can intervene in proceedings before the FPC as a matter of right, and the Commission has no power to exclude it, *Public Service Commission of New York* v. *FPC;* 295 F. 2d 140 (D.C. Cir. 1961), cert. den. sub. nom. *Shell Oil Company* v. *Public Service Commission of New York*, 368 U.S. 948; 7 L. ed 2d 343; 82 S. Ct. 388.

[15] 34 FPC 189; affirmed in part, reversed in part; *Skelly Oil Company* v. *FPC*; — F. 2d —; Case No. 8385 *et al.*, decided January 20, 1967.

[16] *El Paso Natural Gas Co.*, 35 FPC 40, appeals pending in 10th Cir.; *Phillips Petroleum Co.* v. *F.P.C.*, Case No. 8723, *et al.*

Conclusion

A square conflict between two Circuit Courts of Appeals requires determination by this Court of the basic issue whether the Commission's discretion to determine the price "line" is limited only to its own past actions, or whether it may continue to adjust the line as "current conditions" require. The future of the ability of the natural gas industry in the United States to maintain adequate supplies for the consumer may well hinge on this Court's decision.

Respectfully submitted,

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April 21, 1967.

UNITED STATES COURT OF APPEALS

FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 19,796

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
PETITIONER,

v.

FEDERAL POWER COMMISSION, RESPONDENT

SUN OIL COMPANY,
SKELLY OIL COMPANY,
CALLERY PROPERTIES, INC.,
SHELL OIL COMPANY,
PAN AMERICAN PETROLEUM CORPORATION,
SUPERIOR OIL COMPANY,
HUMBLE OIL & REFINING COMPANY,
W. S. KILROY, et al., and KILROY PROPERTIES, INC.,
H. L. HAWKINS & H. L. HAWKINS, JR.,
PLACID OIL COMPANY, et al.,
INTERVENORS

No. 19,800

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK
PETITIONER,

v.

FEDERAL POWER COMMISSION, RESPONDENT

MONSANTO COMPANY
MRS. JAMES R. DOUGHERTY, et al., W. A. STOCKARD,
et al., EDWIN M. JONES OIL COMPANY,
SHELL OIL COMPANY,

H. D. Bruns & MPS Production Company,
Continental Oil Company,
Lamar Hunt,
intervenors

No. 19,919

Long Island Lighting Company, petitioner

v.

Federal Power Commission, respondent

Lamar Hunt,
Mrs. James R. Dougherty, et al., W. A. Stockard, et al., Edwin M. Jones Oil Company,
intervenors

No. 19,941

Continental Oil Company, petitioner

v.

Federal Power Commission, respondent

No. 19,957

The Superior Oil Company, petitioner

v.

Federal Power Commission, respondent

On Petitions to Review Orders of the Federal Power Commission

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Decided February 7, 1967

Mr. Morton L. Simons, with whom *Mr. Kent H. Brown* was on the brief, for petitioner in Nos. 19796 and 19800.

Mr. Joseph C. Johnson, of the bar of the Supreme Court of Texas, *pro hac vice,* by special leave of court, with whom *Messrs. Bruce R. Merrill* and *Thomas H. Burton* were on the brief, for petitioner in No. 19941.

Mr. Homer J. Penn for petitioner in No. 19957. *Messrs. Herbert W. Varner* and *William T. Kilbourne, II,* were on the brief for petitioner in No. 19957.

Mr. Joel Yohalem, Attorney, Federal Power Commission, with whom *Messrs. Richard A. Solomon,* General Counsel, and *Howard E. Wahrenbrock,* Solicitor, Federal Power Commission, were on the brief, for respondent.

Mr. Sherman S. Poland, with whom *Mr. Donald B. Robertson* was on the brief, for intervenor Skelly Oil Company in No. 19796, argued on behalf of all intervenors. *Mr. Oliver L. Stone* was on the brief for intervenor Shell Oil Company. *Mr. Richard F. Generelly* was on the brief for intervenors Callery Properties, Inc., H. L. Hawkins, H. L. Hawkins, Jr., and Monsanto Company. *Mr. J. Evans Attwell* was on the brief for intervenor W. S. Kilroy, et al. *Mr. James K. Schooler* was on the brief for intervenor Humble Oil & Refining Company. *Messrs. Carroll L. Gilliam* and *Philip R. Ehrenkranz* were on the brief for intervenor Pan American Petroleum Corporation. *Messrs. Bernard A. Foster, Jr.* and *Donald B. Robertson* were on the brief for intervenors Mrs. James R. Dougherty, et al., Edwin M. Jones Oil Company and W. A. Stockard, et al. *Messrs. Morton L. Simons* and *Bertram D. Moll* also entered appearances for petitioner in No. 19919. *Mr. Robert E. May* also entered an appearance for intervenor Skelly Oil Company. *Mr. Robert W. Henderson* also entered an appearance for intervenor, Lamar Hunt.

Before BAZELON, *Chief Judge,* WILBUR K. MILLER, *Senior Circuit Judge,* and TAMM, *Circuit Judge.*

BAZELON, *Chief Judge*: We are to review a Federal Power Commission (FPC) order certificating sales of natural gas from producers to interstate pipelines. The sales were certificated in the *Hawkins* (Texas Railroad District No. 3)[1] and *Sinclair* (Texas Railroad District No. 2)[2] proceedings, which are consolidated here.

The New York Public Service Commission challenges the certificates on three grounds. First, there was no showing of public need for the gas. Second, the "in-line" price was too high. And third, the FPC erroneously postponed deciding whether the producers should be required to refund amounts in excess of the in-line level which were collected under a temporary certificate. Superior and Continental (producers) challenge the in-line price as too low. Superior claims also that the FPC set too high an interest rate on funds which would be retained by the producers in excess of the amount allowed by the permanent certificates. The intervenors support the FPC's determinations, although some of them think that the in-line price should have been higher.

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The Public Need for the Gas

We face some confusion about whether New York properly raised the issue of public need. At the prehearing conference in the *Hawkins* proceeding, New York limited the issue to whether or not the *pipelines* needed the gas.[3]

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[1] *H. L. Hawkins & H. L. Hawkins, Jr. (Operator), et al.* Docket Nos. G-18077, *et al.*

[2] *Sinclair Oil & Gas Company, et al.* Docket Nos. G-16760, *et al.*

[3] H.A. (*Hawkins* Joint Appendix) 7-19.

However, in its exceptions to the Examiner's initial decision New York said, "In view of (a) the absence of any evidence of public need for the gas and (b) the many indications that pipelines in the Gulf Coast area are presently suffering from take-or-pay problems,[4] the application should be denied."[5] This raised the issue of the *public's* need for the gas. New York used the take-or-pay problems to alert the FPC to a potentially harmful situation and obligate it to give reasons why, in spite of those problems, the sales should be certificated.[6] New York reiterated its position in a petition for rehearing before the FPC.[7]

In *Sinclair,* New York raised the issue in the same terms as in the *Hawkins* proceeding.[8] And again, after the FPC refused to consider the issue, New York repeated its contentions in a petition for rehearing.[9] Since New York presented the issue of public need in its petition for rehearing in both the *Hawkins* and *Sinclair* proceedings, our review is authorized by Section 19(b) of the Natural Gas Act.[10]

The most obvious element of public necessity is the demand for the gas. In several cases decided before CATCO, the existence of an unsatisfied market was considered of great importance. For example, in *Oklahoma Natural Gas*

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[4] New York claimed that the pipelines were obligated to take or pay for more gas than they could use. [Footnote added.]

[5] H.A. 268.

[6] This argument is analogous to the argument that the FPC must give reasons why a certificate should be granted even though the price is out of line. The out-of-line price alerts the FPC to the potentially harmful situation. See *Atlantic Refining Co.* v. *Public Service Commission,* 360 U.S. 378 (1959) (CATCO).

[7] H.A. 311-12.

[8] S.A. (*Sinclair* Joint Appendix) 198.

[9] S.A. 243-44.

[10] 15 U.S.C. § 717r (b) (1964).

Co. v. *Federal Power Commission*[11] the court allowed the need in the Chicago market to outweigh even considerations of the price of the gas. And in *United Gas Improvement Co.* v. *Federal Power Commission*,[12] because the demand for the gas was shown to be great, the court did not insist that the FPC regulate the initial price.[13]

Since these cases were decided, the Supreme Court has held, in CATCO, that the initial price is extremely important. But CATCO does not suggest that the public's need for the gas is irrelevant. Indeed, the Court seems to have imposed on the producer the burden of proving public need before certification. In part, the Court reversed the Commission's certification in CATCO because there was no "support whatever in the record for the conclusory finding on which the order was based that 'the public served through the Tennessee Gas System is greatly in need of increased supplies of natural gas.' "[14]

But market demand is not the only relevant factor. In the *Transco* case,[15] the question was whether the FPC, "through its certification power, may prevent the waste of gas committed to its jurisdiction."[16] The Supreme Court said "no one [disputed] that natural gas is a wasting resource and that the necessity for conserving it is paramount."[17] The dispute was whether the "public conven-

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[11] 103 U.S.App.D.C. 256, 257 F.2d 634, *cert. granted,* 358 U.S. 877 (1958), *cert. dismissed,* 358 U.S. 948 (1959).

[12] 269 F.2d 865 (3d. Cir.), *vacated sub nom. Public Service Commission* v. *Federal Power Commission,* 361 U.S. 195 (1959).

[13] See also *Department of Conservation* v. *Federal Power Commission,* 148 F.2d 746 (5th Cir.), *cert. denied* 326 U.S. 717 (1945), in which the court allowed the need for the gas to outweigh evidence that the gas was going to be put to an inferior use.

[14] *Supra* note 6, at 393.

[15] *Federal Power Commission* v. *Transcontinental Gas Corp.*, 365 U.S. 1 (1961).

[16] *Id.* at 8.

[17] *Ibid.*

ience and necessity," referred to in § 7(e) of the Natural Gas Act, included considerations of conservation, or whether the FPC was precluded from considering that factor. In affirming the Commission's action, the Court decided that conservation was relevant to public convenience and necessity. *Transco* was a pipeline certificate case, and the instant case is a producer certificate case. But pipelines and producers are certificated under the same statute, and, at least without strong evidence, we should not say that conservation is relevant in one case and not in the other. The public's interest in conserving gas is no less when the applicant for a certificate of public convenience and necessity is a producer.

The parties do not explicitly deny the relevance of market demand and conservation, but we are asked to disregard the issue of public need for four other reasons. First, it was not properly raised below. We have already dealt with that argument. Second, the public need for the gas should be determined in a pipeline certificate or pipeline rate case, not in a producer certificate case. Third, the FPC can postpone consideration of public need until it completes its pending rule-making proceeding on the problem of take-or-pay contracts. And fourth, "because of the nature of the gas business and the obligation of pipeline companies to the consuming public, it is to be expected that such companies will occasionally have long-term contracts for supplies which will give them gas for future, even though the supplies may be slightly in excess of their present-day needs."[18] We will deal with the last three contentions in turn.

1. According to New York, the issue of public need should not be decided only in a pipeline certificate or rate case. New York argues that if the gas is sold to a pipeline which is unable to use it, and if the pipeline must either take the gas or pay for it nonetheless, then

[18] H.A. 280.

the loss sustained by the pipeline will be reflected in the price charged to the public utility and ultimately in the price charged to the consumer. The FPC could eliminate this problem by ruling that the pipeline's investment in the unused gas was "imprudent" and refusing to allow the pipeline to add its cost to the rate base. However, the FPC has cited no case in which the cost of unused gas was eliminated from the rate base. To the contrary, there is some indication that the FPC may be allowing at least part of the loss to be shifted to the consumer.[19] Indeed, it would seem difficult for the FPC first to certificate a sale to a pipeline and then to claim that the pipeline's investment in the gas was imprudent.

Regardless of how the FPC uses its "imprudent investment" doctrine, there is another reason why the public's need for the gas must be considered in a producer certification. As we have indicated, the FPC must prevent waste of natural gas. One of the most important ways is to control and limit the end uses of gas.[20] The FPC must compare various uses and determine which ones are more economically necessary. If the proposed sale is to a consumer who will use the gas in an economically "inferior" way then the sale is not certificated. Of course, to do the job properly the FPC must consider *all* alternative uses.[21] It recognizes this responsibility in pipeline certificate cases.[22] But if it refuses to consider the issue in producer certificate cases and waits for pipeline cases, some of the alternatives will already have been eliminated.

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[19] See *United Gas Pipe Line Co.*, 31 FPC 1180, 1191-92 (1964), and *United Gas Pipe Line Co.*, 32 FPC 1515, 1519 (1964).

[20] *Federal Power Commission* v. *Transcontinental Gas Corp.*, *supra* note 15, at 8.

[21] "[Section] 7(e) requires the Commission to evaluate *all* factors bearing on the public interest." *Atlantic Refining Co.* v. *Public Service Commission, supra* note 6, at 391. [Emphasis added.]

[22] *Federal Power Commission* v. *Transcontinental Gas Corp.*, *supra* note 15.

In the pipeline case the FPC can direct the gas towards one rather than another of the pipeline's customers but without considering the customers of other pipelines which might have bought the gas. Thus, the gas may go ultimately to consumers whose use will be less economically beneficial than the use of other potential purchasers.

Because the FPC refused to consider the issue of need, this record does not indicate whether or not this gas has been wasted.[23] However, such wasting is a possible result of the alleged oversupply situation of some of the pipelines here.[24] The possibility that gas may be wasted requires that the FPC determine the issue of need *before* the initial sale to a pipeline. Otherwise it may be too late to protect the public interest.[25]

2. The FPC argues that "insofar as there may be any [take-or-pay] problem for [the pipelines in the instant case], it is one not peculiar to them and may therefore be resolved . . . by the Commission's reservation of the matter for consideration in the pending rulemaking proceeding on that subject. . . ."[26] As we have noted, though, the take-or-pay problem does not exhaust the considerations relevant to an informed decision about the public's need for the gas. It is unlikely that any decision the Commission makes in its rule-making proceeding would deal with the entire "need" issue. The rule-making proceeding on which the FPC relies

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[23] We do not know whether anyone else could have taken the gas, or, if so, whether he served markets which would differ from the markets served by the pipelines here.

[24] There is a suggestion that the gas involved in this case was obviously needed because some of it has already been consumed. The issue of need, however, is not decided simply because someone will consume the gas. The real questions are whether the consumer was forced, or will be forced, to pay more for the gas because of the pipeline's poor take-or-pay situation and whether the gas could have been put to a superior use.

[25] See *City of Pittsburgh* v. *Federal Power Commission*, 99 U.S.App.D.C. 113, 237 F.2d 741 (1956).

[26] Brief for Respondent, p. 29.

has been pending for five and a half years,[27] and we do not know when a decision will be reached. We can only speculate about what that decision will be and how it will apply to the question of public need. We think such an uncertain proceeding should not excuse the Commission from its present responsibilities.[28]

3. The FPC's last argument is that the "nature of the gas business and the obligation of pipeline companies to the consuming public" sometimes require a poor take-or-pay situation.[29] If this means that other considerations may outweigh the pipeline's poor take-or-pay situation, we agree. And these considerations may also outweigh the considerations of conservation inherent in the case. But there is no evidence in the record which indicates what these considerations are or how they are relevant to this certification. If public convenience and necessity requires this certification, this must appear from something more than the FPC's broad and unsupported statement about the "nature of the gas business" in a case where the FPC thought the issue irrelevant.[30]

Although we remand this case so that the FPC can consider the issue of public need, we recognize an obvious ten-

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[27] Docket No. R-199, 26 Fed. Reg. 4615 (May 22, 1961).

[28] See *Public Service Commission* v. *Federal Power Commission,* 117 U.S.App.D.C. 287, 292-93, 329 F.2d 242, 247-48, *cert. denied sub nom. Prado Oil & Gas Co.* v. *Federal Power Commission,* 377 U.S. 963 (1964). A day before this opinion was issued, we were informed that the FPC completed its rule-making proceeding on January 18, 1967. The new rule does not affect our decision to remand this case for a determination of public need. That rule is subject to further review. In any event, we think the FPC should decide, in the first instance, how the new rule relates to the issue of whether the public needs the gas involved in this case. Therefore, on the remand we order herein, the FPC will make that determination according to the principles stated in this opinion. See discussion following note 30 *infra.*

[29] H.A. 280.

[30] In CATCO the Supreme Court also rejected an unsupported statement about the public need. *Supra* note 6, at 393.

sion between the statutory requirement that it do so and administrative feasibility. The public convenience and necessity includes many considerations, but if there is to be any effective certification of producers the FPC must sometimes stop short of the ideal.[31] It is evident, too, that the FPC must have great latitude in its choice of procedures. We are not demanding that the FPC hold a long and complex hearing in each of its many producer application cases. But it does not seem too difficult to have the producer's customers or the pipeline's customers testify about the take-or-pay situation.[32] Regarding the broader aspects of the "nature of the gas business" or of conservation, the FPC may consider studies of its staff. It may, after study, issue policy statements. These studies or statements may be relevant to large geographic areas, or perhaps to the whole gas industry. Then it would not be necessary to relitigate need in each case; the FPC need only show that the broad statement or study covers the particular certification before it. In short, we do not now prescribe any particular method for deciding need. Nor is our discussion of what public need means exhaustive. We decide only that when a party makes a non-frivolous claim that there is no public need for the gas the FPC must give considered reasons if it decides otherwise. Its decision must be made *before* it grants a

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[31] *Cf. United Gas Improvement Co.* v. *Callery Properties,* 382 U.S. 223 (1965). *Callery* does not apply directly though. There, no one doubted the need for the gas. The dispute was over the price. The longer it took to set the price, the more the consumer was hurt. Understandably, the Supreme Court wanted the Commission to act quickly and efficiently. The entire purpose of the Act is to protect the consumer. Here, New York claims that this sale should not be certificated at all, no matter at what price and no matter how quick the procedure. It is counter-productive to streamline procedure when the effect is to prevent the Commission from considering the possibility that the sale itself would not be in the public interest.

[32] Or perhaps the Commission can rely upon a previously decided producer or pipeline certificate case if the decisions there are relevant to the applications pending before the Commission.

permanent certificate to a producer.[33] "[A] certificate shall be issued . . . authorizing the . . . sale . . . if . . . the proposed . . . sale . . . is or will be required by the present or future public convenience and necessity; otherwise such application shall be denied."[34]

II

The In-Line Price

The second major dispute in this case concerns the FPC's determination of the in-line price. Since the CATCO decision, the FPC has been granting permanent certificates of public convenience and necessity only if the price of the gas is in-line. The question is, in line with what? Judging from these and other FPC proceedings, the "line" is determined as follows: First the Commission chooses a time period and a geographical area which it considers relevant[35] and lists all the prices at which gas was sold at that time and in that area. Then it eliminates prices which are "suspect" either because they are presently under litigation or Commission review or because they are similar to a price under a cloud.[36] When the price array is completed the FPC makes several calculations, for example, the average price, the median price,

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[33] *Cf. Federal Power Commission* v. *Texaco,* 377 U.S. 33, 42-44 (1964), and *Federal Power Commission* v. *Hunt,* 376 U.S. 515, 525-26 (1964).

[34] 15 U.S.C. § 717f(e) (1964).

[35] Here the area for the *Hawkins* proceeding was Texas Railroad District No. 3, and the area for the *Sinclair* proceeding was Texas Railroad District No. 2. In both proceedings there were two relevant time periods—in *Hawkins* from January 1, 1958, to September 28, 1960, (pre-Policy Statement period), and from September 28, 1960, to January 1, 1964, (post-Policy Statement period), and in *Sinclair* from January 1, 1957, to September 28, 1960, (pre-Policy Statement period), and from September 28, 1960, to March 10, 1964, (post-Policy Statement period).

[36] See, *e.g., United Gas Improvement Co.* v. *Federal Power Commission,* 283 F.2d 817 (9th Cir. 1960), *cert. denied sub nom. Superior Oil Co.* v. *United Gas Improvement Co.,* 365 U.S. 879 (1961).

the weighted average price, and the price at which substantial volumes of gas flowed in interstate commerce. The FPC adjusts some of these prices by assigning differing weights to the various prices which form the price array. At least one Commissioner in our case gave some weight also to a guideline price announced first in 1960 and subsequently revised.[37] The Commission considers these weights and the adjustments, and then picks a price.[38] Here the Commission set the in-line price at 15¢ per Mcf for District No. 2 during the period before the Policy Statement (September 28, 1960) and at 16¢ for the post-Policy Statement period.[39] For District No. 3, the prices were 16¢ and 17¢ respectively.

The petitioners have many disagreements with what the FPC did in this case. Continental and Superior think the Commission should have given more weight to certain 20¢ sales which were permanently certificated, to sales which were temporarily certificated, and to contract prices even before these prices are tested in any kind of certificate proceeding.[40] They also claim that the Commission erroneously considered certain sales at 14¢ and less, erroneously excluded intrastate sales, and erroneously used estimated rather than actual volumes when calculating weighted average prices. In short, they claim that the Commission acted arbitrarily and without any recognizable standards.

New York claims that the FPC should have given no weight to contract prices or to sales made pursuant to

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[37] See Commissioner Bagge's concurring opinion in *Hawkins*. H.A. 297.

[38] The proceedings in this case provide some examples of the Commission's methods. See the appendix attached to this opinion.

[39] The pre- and post-Policy Statement periods are described fully in note 35 *supra*.

[40] Their claim that the Commission disregarded these prices cannot be based on the record in this case. See, *e.g.*, S.A. 226 and H.A. 285-86 quoted in the appendix *infra*. The producers' claim is reduced to the contention that not enough weight was given.

temporary certificates, and that it erroneously considered certain permanently certificated prices. New York says these permanently certificated prices were incorrectly determined and therefore should not be allowed to affect subsequent in-line prices.

To properly weigh these claims we must understand the purpose of in-line pricing.

In-Line Pricing

The concept of an in-line price is an artificial one created by the Supreme Court, the Courts of Appeals, and the Commission for the sole purpose of protecting the consumer. Before the concept existed, the FPC usually proceeded in the following way. A producer who wanted to sell gas in interstate commerce applied to the Commission for a certificate of public convenience and necessity under § 7 of the Act. When the certificate was granted, the producer-seller and the pipeline-buyer executed the sale at a price which they had already negotiated. If that price was too high, the FPC, either on its own motion or acting on the complaint of an interested party, could institute proceedings under § 5 of the Act to determine the "just and reasonable" price, after which the producer was forced to lower his price accordingly. However, since § 5 does not provide for refunds, the producer was allowed a "windfall" (with a consequent "squall" for the consumer) during the period between commencement of the sales and the conclusion of the hearing under § 5.[41] Section 5 hearings were long and complicated, and the windfall could be quite large. The ordinary protections of the market place did not exist in this regulated monopoly industry. The producer, of course, was interested in extracting the highest price from the buyer. But the buyer did not have an equal interest

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[41] *Atlantic Refining Co.* v. *Federal Power Commission, supra* note 6, at 390.

in keeping the price down because the price he paid became part of his rate base and was ultimately paid by the consumer.[42] Presumably the consumer did not have any choice except to buy the fuel at the price which was set.[43]

The procedure after the invention of in-line pricing changed in one significant way. Now, when the FPC grants a certificate of public convenience and necessity, a price condition is usually attached. A dissatisfied producer who wants to sell at a higher price can file a new rate schedule under § 4 of the Act subject to his contract with the pipeline.[44] These rates become effective after thirty days unless challenged by the FPC. Even if challenged, the new rates become effective after five months if the Commission has not completed its "just and reasonable" determination by that time. Eventually, then, the producer may charge whatever price he wants.[45] However, by filing under § 4, the producer becomes subject to payment of refunds if the FPC later finds that the price charged was not just and reasonable. In this way, the consumer is afforded at least some protection against excessive prices.[46]

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[42] *Atlantic Refining Company* v. *Federal Power Commission,* 115 U.S.App.D.C. 26, 28 at n. 11, 316 F.2d 677, 679 at n. 11, (1963).

[43] *United Gas Improvement Co.* v. *Federal Power Commission,* 290 F.2d 133, 135 (5th Cir.), *cert. denied sub nom. Sun Oil Co.* v. *United Gas Improvement Co.,* 368 U.S. 823 (1961).

[44] *Cf. Texaco* v. *Federal Power Commission,* 290 F.2d 149, 156 (5th Cir. 1961).

[45] The Commission may, however, impose a temporary moratorium on price increases. See *United Gas Improvement Co.* v. *Callery Properties, supra* note 31. A price moratorium was imposed in the instant case, but it is not before us on appeal.

[46] The Act was so framed as to afford consumers a complete, permanent and effective bond of protection from excessive rates and charges. *Atlantic Refining Co.* v. *Public Service Commission, supra* note 6, at 388.

The Use of Contract Prices

From the description of in-line pricing it is evident that the FPC cannot use the prices at which producers and pipelines contract as a basis for setting the price. The need for the FPC, and for a concept like in-line prices, arises primarily because the unregulated market place cannot protect the consumer adequately. Congress created the FPC to protect the consumer from the market place, not simply to reflect it. The Commission should not rely upon prices over which it has not exercised careful control.[47]

One Court of Appeals has viewed the Commission's reliance on contract prices as the reason for the CATCO opinion.

> [W]e perceive that most of the Commission's approach to the certification procedures, until stopped by the Supreme Court in CATCO, was subject to the [following] criticism . . .: that the Commission was permitting the initial filing prices to be fixed by the producers merely on a showing, *so far as price justification was concerned*, that they had been bargained for at arm's length, or that they were not higher than a price someone else was then paying in the area.[48]

And this court has been wary of allowing the Commission to avoid its responsibility by relying on prices negotiated in the market place.[49]

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[47] See *Atlantic Refining Company* v. *Federal Power Commission*, *supra* note 42, at 28, n. 11, 316 F.2d at 679, n. 11.

[48] *United Gas Improvement Co.* v. *Federal Power Commission*, *supra* note 43, at 135-136. [Emphasis in the original.] See also *United Gas Improvement Co.* v. *Federal Power Commission*, 290 F.2d 147, 148 (5th Cir.), *cert. denied sub nom. Superior Oil Co.* v. *United Gas Improvement Co.*, 366 U.S. 965 (1961).

[49] *Public Service Commission* v. *Federal Power Commission*, 109 U.S.App.D.C. 289, 291, 287 F.2d 143, 145 (1960), and *Public Service Commission* v. *Federal Power Commission*, 109 U.S.App. D.C. 292, 296, n. 4, 287 F.2d 146, 150, n. 4 (1960), *cert. denied sub nom. Hope Natural Gas Co.* v. *Public Service Commission*, 365 U.S. 880 (1961).

The Use of Temporary Certificates and the Policy Statement

If the Commission relies on prices over which it has never exercised control, it effectively abdicates its responsibility to protect consumers. Although prices contained in temporary certificates are not completely without Commission control, neither are they subjected to thorough consideration. According to the statute, temporary certificates are granted only "in cases of emergency" pending determination of an application for a permanent certificate. Temporaries are granted in *ex parte* proceedings "without notice or hearing."[50] No record is made, so it is impossible for a court to know on what basis the Commission granted the certificate. Accordingly, standards on review are minimal. This court has upheld a temporary certificate although we admitted that the summary nature of the proceeding precluded us from passing intelligently upon the parties' contentions.[51]

Recently, though, the FPC has attempted to make temporary certification a more considered decision. In 1960 it promulgated a Policy Statement which included guideline prices beyond which it would not certificate sales, even temporarily. In theory, the Policy Statement could justify inclusion of temporary certificates in the permanent certificate price array, since the Policy Statement could provide some degree of intelligent control over temporary prices.

In fact, however, the Policy Statement has not had a curative effect. The FPC itself seems to give the Statement very little (and very ambiguous) weight. In its first

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[50] 15 U.S.C. § 717f(c) (1964).

[51] *Public Service Commission* v. *Federal Power Commission,* 117 U.S.App.D.C. 195, 199, 327 F.2d 893, 897 (1964). See also *American Liberty Oil Co.* v. *Federal Power Commission,* 301 F.2d 15 (5th Cir. 1962). And see *Public Service Commission* v. *Federal Power Commission, supra* note 28, at 294, 329 F.2d at 249, in which this court characterized temporary certificates as being "without notice or hearing or mature consideration."

statement, the FPC said that "these price levels . . . . are for the purpose of guidance and initial action by the Commission and their use will not deprive any party of substantive rights."[52] When the State of Wisconsin petitioned this court to review the Policy Statement, the FPC moved for dismissal on the ground that the Policy Statement "does not modify the procedures under which certificates are granted. . . . It denies no rights and imposes no obligations."[53] We agreed and dismissed Wisconsin's petition for review.[54] The Commission has repeatedly held that the Policy Statement does "not purport to fix the 'in-line' price."[55] And recently the Commission characterized the guideline prices as being relevant only when "no protests or petitions to intervene [are] filed" in the certification proceeding.[56] In the instant case, only one Commissioner relied upon the guideline prices; two ignored them, and two felt that reliance upon the Policy Statement would be impermissible.

Further, we cannot know whether the guideline price actually controls temporary prices unless we know what the guideline price is based on. For example, it is conceivable that temporary certificates have significant influence upon the guideline price. If so, the guidelines do not control temporary prices. In any event, it is impossible to determine how the guidelines were set. The Commission listed a number of very general factors but was not specific about what the factors were or how they were considered. When

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[52] 24 FPC 818, 819 (1960).

[53] *Wisconsin* v. *Federal Power Commission,* No. 16118 Motion to Dismiss, p. 2 (1961).

[54] *Wisconsin* v. *Federal Power Commission,* 110 U.S.App.D.C. 260, 292 F.2d 753 (1961).

[55] *Amerada Petroleum Corp.,* 29 FPC 171, 172 (1963), *Union Texas Petroleum,* 29 FPC 273, 275 (1963), *Union Texas Petroleum,* 29 FPC 733, 734 (1963).

[56] 30 Fed. Reg. 4670, 4671 (1965). See also *Amerada Petroleum Corp., supra* note 55, at 172 and *Union Texas Petroleum,* 29 FPC at 275 (1963).

asked, the FPC refused to disclose the basis for its determination.[57]

A still more persuasive reason for eliminating temporary prices from the permanent price array is the way their use may injure consumers. The effect may be a slow escalation of in-line prices: An in-line price is set; the guideline price is set somewhat higher; temporary certificates are granted at the guideline price; the new temporary certificates are used in determining a new in-line price, which will be higher than the first in-line price; the new in-line price raises the guideline price; and then the spiral begins again. Although, in fact, we cannot isolate so clearly the effect of the temporaries and the guidelines, there can be no doubt that an escalation has occurred, and in a manner similar to the process described.[58] This process contradicts CATCO's admonition to hold the line in the interim period between the sale of gas and the determination of just and reasonable rates. According

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[57] See, *e.g.*, Nos. 7781, *et al.*, *Sunray DX Oil Co.* v. *Federal Power Commission,* (10th Cir. Dec. 9, 1966), Op. pp. 15-19; *Amerada Petroleum Corp., supra* note 55.

[58] In *Texaco Seaboard,* 29 FPC 593 (1963), the Commission found the Texas Railroad District No. 3 in-line price to be 16¢ for the period preceding September 28, 1960. At the same time, the Commission set its guideline price at 17¢. 29 FPC 590 (1963). Now the Commission finds that the in-line price for District No. 3 has jumped to 17¢.

In *Hassie Hunt Trust,* 30 FPC 1438 (1963), the Commission found the District No. 2 in-line price to be 15¢ for the period preceding September 28, 1960. At the same time, the Commission set its guideline price at 16¢. 30 FPC 1435 (1963). Now the Commission finds that the in-line price for District No. 2 has jumped to 16¢.

In *Skelly Oil Co.,* 28 FPC 401 (1962), the Commission found the District No. 4 in-line price to be 15¢ for the period preceding September 28, 1960. At the same time, the Commission set its guideline price at 16¢. 28 FPC 441 (1962). Recently the Commission found that the in-line price for District No. 4 has jumped to 16¢. See *Sunray DX Oil Co.* v. *Federal Power Commission, supra* note 57.

to CATCO, one reason why the consumer needs protection during the interim period is that the period is often long.[59] Under the present administration of the in-line price doctrine the amount of protection for the consumer decreases as the length of the interim period increases. The longer it takes to determine a just and reasonable price, the higher the in-line price becomes, and the consumers' potential refund drops accordingly.

There is a final, and completely separate, reason why temporary prices should not affect the in-line price. The first court to discuss in-line prices held that prices which were suspect because they were under a cloud of court or Commission review could not be used in the permanent price array.[60] Since then almost every court,[61] including the Supreme Court,[62] has accepted the suspect price doctrine. The suspect price doctrine clearly includes temporarily certificated prices. Temporarily certificated prices may be, and often are, changed by the Commission. They are "subject to judicial review."[63] Prices that are so particularly subject to the hazard of change do "not provide a reasonably reliable basis upon which to predicate a price line."[64] And, acceptance of temporarily certificated prices has, in fact, had the effect of "creating a standard by which the questioned rates [are] judged."[65]

The producers argue, contrary to our holding, that temporarily certificated prices and contract prices must

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[59] *Supra* note 6, at 389.

[60] *United Gas Improvement Co.* v. *Federal Power Commission, supra* note 36.

[61] See, *e.g., Public Service Commission* v. *Federal Power Commission,* 109 U.S.App.D.C. 292, *supra* note 49 and *Public Service Commission* v. *Federal Power Commission, supra* note 28.

[62] *United Gas Improvement Co.* v. *Callery Properties, supra* note 31, at 227.

[63] *Ibid.*

[64] *United Gas Improvement Co.* v. *Federal Power Commission, supra* note 36, at 824.

[65] *Ibid.*

influence the in-line price. They rely on suggestions in some opinions that the line should "reflect current conditions in the industry."[66] This argument was adopted recently by the Tenth Circuit in *Sunray DX Oil Co.* v. *Federal Power Commission*[67] which held that it is permissible for the FPC to consider temporaries and contract prices.

However, the Tenth Circuit was faced with a problem very different from ours. There, only 1.39% of the gas sold in the area was permanently certificated.[68] On this basis the court refused to apply the suspect price doctrine and approved the FPC's method of determining the in-line price. "[W]hen no appreciable volume of gas is moving under permanent certificates, the Commission has nothing upon which to base a decision as to in-lineness unless it turns to the temporaries."[69] In our case there is a substantial volume moving under permanent certificates.[70] We are not reviewing the FPC's method of determining an in-line price when there are no permanently certificated prices available for comparison.

Moreover, we cannot accept the reasoning of the Tenth Circuit's opinion as it applies to this case. Temporaries and contract prices do reflect current conditions in the industry because they reflect real dealings in the market place. This recognition, far from justifying reliance upon these prices, provides a reason for disregarding them. As we have noted, the need for in-line pricing arises because the unregulated market place cannot protect the consumer adequately. Reliance on prices over which there has been no careful regulatory control contradicts this need.

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[66] See, *e.g., ibid.*
[67] *Supra* note 57.
[68] *Supra* note 57, at Op. p. 24.
[69] *Supra* note 57, at Op. p. 26.
[70] See, *e.g.,* H.A. 282, 284-86, 299-300; S.A. 220, 223, 226-27.

We are not suggesting, of course, that current conditions are never relevant to the FPC. In a § 4 or § 5 hearing the FPC considers current conditions in order to set a just and reasonable price. However, the courts have already rejected attempts to import standards relevant to § 4 and § 5 hearings into § 7 hearings. For example, in *Callery* the producers tried to introduce economic and financial evidence, but the FPC disregarded it.[71] The Fifth Circuit reversed the Commission. In essence the court said that this evidence was relevant to current conditions in the industry, and that these conditions were relevant to the determination of the in-line price.[72] The Supreme Court rejected this argument summarily. "To consider in this § 7 proceeding the mass of evidence relevant to the fixing of just and reasonable rates under § 5 might in practical effect render nugatory any effort to fix initial prices." [73] In the recent Tenth Circuit case the producers tried to introduce the same kind of evidence. The court responded:

> The producers seek to avoid the impact of Callery by the assertion that the proffered evidence was a streamlined presentation which could not cause any crippling delay. In our opinion, the admissibility of such evidence does not depend on any quantitative test. Relevance is determined by the substance of the offer. Although we agree with the producers that neither CATCO nor Callery establishes any specific evidentiary standards, the point is that the just and reasonable rate standards of §§ 4 and 5 do not apply to § 7 where the test is public convenience and necessity.[74]

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[71] See *Callery Properties* v. *Federal Power Commission*, 335 F.2d 1004, 1009 (5th Cir. 1964), for a description of the evidence.

[72] *Id.* at 1013.

[73] *Supra* note 31, at 227-28. In CATCO the Supreme Court had already recognized the difference between the standards of a § 7 and a § 4 or § 5 proceeding. "[T]he Act does not require a determination of just and reasonable rates in a § 7 proceeding as it does in one under either § 4 or § 5." *Supra* note 6, at 390.

[74] *Supra* note 57, at Op. pp. 14-15.

We think this response, which is properly based on the logic of *Callery* and CATCO, is inconsistent with the same court's acceptance of temporaries and contract prices. If the courts and the FPC will not allow consideration of evidence which shows what the current conditions are, then temporaries and contract prices should not be accepted on the basis that they reflect current conditions.

The purpose, quite simply, of a § 7 proceeding is to protect the consumer until the FPC can determine the just and reasonable rate. This latter determination depends, in part, on current conditions in the industry. The determination of an in-line price should not depend on current conditions unless, in a particular case, there is something special about these conditions which requires the FPC to sacrifice some of the consumer's protection. For example, in a particular case, the FPC may feel that an in-line price which is too low subjects the producers to too much risk. And this risk may endanger investment in the industry. In that event the FPC would have to weigh this danger against the diminution of consumer protection. But the FPC has advanced no such reasons in this case. Here the FPC used temporarily certificated and contract prices in an automatic, arithmetical way to raise the in-line price, without attempting to justify the decrease in consumer protection.

Finally, it is argued that elimination of temporarily certificated and contract prices from the price array will cause a "price-freeze." But our proposed decision will not freeze the price of gas. If the producer is dissatisfied with the in-line price he can file a new, and higher, rate schedule under § 4 of the Act.[75] Neither will our decision permanently freeze the in-line price for an area. We presume that the in-line price will be adjusted after the Commission determines the just and reasonable price. It is true that our decision may cause the in-line price

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[75] See note 45, *supra*.

to be frozen temporarily during the interim period between sales of gas and the rate determination under § 4 or § 5 of the Act. This kind of freeze seems to be required by the logic of CATCO and in-line pricing. But we do not hold that the FPC can never raise the price line in the interim period. We hold only that the Commission has advanced no reason why an escalation is justified in this case.

Other Claims Regarding the In-Line Price

New York argues that the FPC erroneously determined the pre-Policy Statement in-line price for District No. 3, because it gave weight to prices "tainted" by other prices which were permanently certificated in 1956-57. New York thinks these 1956-57 prices were incorrectly certificated "in light of *CATCO* and the subsequent court cases." [76] Although sometimes it may be wise to re-examine certificated prices, we think that the FPC may give weight to permanently certificated prices even if they were certificated under standards later changed by the courts. This area of the law is constantly changing, and if we require the Commission to re-examine earlier certifications whenever there is a new decision, hearings under § 7 will never end. The proper rule was stated by the Ninth Circuit.

> No doubt there are many certificated prices—some under unconditional certificates and others . . . conditioned, some established in contested proceedings and others not contested—which might be different, and lower, if the Commission were passing on them under section 7 today. But this, we think, does not *require,* although it may *permit,* the Commission to disregard them or to give little weight to them in deciding what is an appropriate price line to which to refer.[77]

[76] Brief for Petitioner, p. 27.

[77] *California* v. *Federal Power Commission,* 353 F.2d 16, 23 (1965). [Emphasis in the original.]

Though the FPC is not required to re-examine permanently certificated prices, neither is it required to include a price in the price array simply because the price was sanctioned in a permanent certificate. The Commission may ignore a price if it has a good reason to do so.[78] In this case, over Superior's objection, the Commission refused to give full weight to certain 20¢ sales. According to the FPC these and similar sales should be discounted because "they either have subsequently been set aside . . . or would have been set aside . . . save for the procedural defect in the PSC review action."[79] This reason is adequate, and we do not think the Commission abused its discretion by not giving full weight to the 20¢ sales.

Lone Star Gathering Company

New York claims that Lone Star is a gathering company rather than a pipeline, and therefore sales to Lone Star should be certificated at the in-line price less the cost of gathering. Since oral argument we have been informed that in Opinion No. 505 the FPC granted Lone Star and United Gas Pipe Line Company permission to consolidate some of their facilities.[80] The FPC was to rehear that case beginning December 6, 1966.[81] Since we do not know what effect the Commission's final decision will have on the issue before us, we reserve decision on New York's claim.

We need not deal with any of the other contentions regarding the in-line price. Some of the parties may now wish to abandon some of their claims. On remand the FPC can deal with the remaining claims according to the principles announced in this opinion.

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[78] A price which is not "comparable" is not considered even if it is permanently certificated. See *United Gas Improvement Co. v. Federal Power Commission, supra* note 36, at 823.

[79] H.A. 284.

[80] *Lone Star Gas Company, et al.*, Docket Nos. CP65-118, *et al.*, issued August 22, 1966.

[81] Order issued October 14, 1966.

III

Refunds

New York argues that the FPC erroneously postponed a decision about whether the producers must refund amounts which were collected, pursuant to temporary certificates, in excess of the in-line level set in the permanent certificate. The FPC answered that it had been awaiting the Supreme Court's action in the *Callery* case which was not decided until December of 1965.[82] According to the FPC's brief, its decision in this case "should be forthcoming in the near future" now that the Supreme Court has decided *Callery*.[83] The Commission took its promise seriously, and on July 22, 1966, it issued Opinion No. 498 which required refunds from some of the producer-applicants involved in the *Hawkins* proceeding.[84] We may assume that a decision in *Sinclair* will follow.

IV

Interest Rates

Superior attacks the FPC's order which sets interest rates for some refunds at 7% and for others at 4½%. Since Superior did not make this objection in an application for rehearing before the Commission, we cannot deal with the claim.[85] In any event, at least on the record and briefs now before us, the Commission's justification for the 7% interest rate seems reasonable.

The Commission's order will be set aside and the case remanded to the Commission for further proceedings consistent with this opinion.

So ordered.

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[82] *Supra* note 31.

[83] Brief for Respondent, p. 37.

[84] *H. L. Hawkins & H. L. Hawkins, Jr. (Operator), et al.* Docket Nos. G-18077, *et al.* The order was amended in Opinion No. 498-A (December 6, 1966).

[85] 15 U.S.C. § 717r (b) (1964). *Cf. Utah Power & Light Co.* v. *Federal Power Commission,* 339 F.2d 436 (10th Cir. 1964).

WILBUR K. MILLER, *Senior Circuit Judge,* dissents.

APPENDIX

Statements Explaining the Method Used to Determine the in-Line Price

In *Hawkins* the hearing examiner explained his decision in the following terms:

> It will be observed from the foregoing distribution of prices for the period September 28, 1960 through December 31, 1963 [the price array], that the largest concentration of sales occurred at 14 cents and 15 cents per Mcf, and that the largest volumes of gas were sold at or below 15 cents per Mcf—more than 80 percent. The average sales price for the period was approximately 14.67 cents and the average sales price by volume was approximately 15.51 cents per Mcf. In respect to the period January 1, 1958 through September 27, 1960 more than 73 percent of the sales occurred at 16 cents or below and these sales account for more than half the volume. The average sales price for this period is 15.41 cents per Mcf and the average sale price by volume is approximately 16.76 cents per Mcf. When the two periods are combined (January 1, 1958 through December 31, 1963) it is apparent that there are two major concentrations of sales namely at 14 cents and 15 cents and minor concentrations at 13.5, 14.5, 16.2 and 20 cents. The average price of the 94 sales is 15.11 cents per Mcf and the average by volume is 16.43 cents per Mcf.
>
> In view of the foregoing and the evidence adduced there is ample support for finding that 16 cents per Mcf at 14.65 psia is an appropriate "in line" price applicable to producer contracts in this proceeding for the period prior to September 28, 1960. The Staff witness found, however, that 16.2 cents was the appropriate "in line" price applicable to the period following September 28, 1960 and in doing so stressed the significance of the sales which were made at 16.2 cents per Mcf. (Four sales before September 28, 1960 and three afterwards.) We do not think that

this is decisive. Indeed there is evidence which tends to show that a higher price may be justified for the pre-Policy Statement period than for the post-Policy Statement period.

It is manifest that the "in line" price is neither the highest price nor the lowest price at which gas is sold from a particular area in interstate commerce. It is also clear that it is not the general average of prices at which gas is sold in a particular period or indeed the mathematical weighted average. Consideration necessarily must be given, however, to the number of sales as well as to the volume—large volumes frequently selling at higher prices than low volumes. Consideration should be given to numerous factors depending upon individual circumstances from one case to another. Consideration must also be given to the Commission's Statement of General Policy No. 61-1, and to policy of the Natural Gas Act as heretofore construed by the Commission and by the courts particularly by the United States Supreme Court in the CATCO case. *Atlantic Refining Co.* v. *P.S.C.*, 360 U.S. 378. In view of these factors and all the facts of record we conclude that the subject sales in this proceeding from the Texas Railroad District No. 3 made under contracts executed both before and after the Policy Statement dated September 28, 1960 should be conditioned at a price no greater than 16 cents per Mcf at 14.65 psia. H.A. 248-50.

When the Commission reviewed the examiner's initial decision, it explained the method as follows:

For the pre-Policy Statement period we agree with the examiner that 16 cents per Mcf . . . is the appropriate in-line price. . . . As can be seen from the table above [the price array], there are comparatively large volumes of gas sold at the 16.0 and 16.2-cent levels, small volumes at 17.5 and 18.0, and very large volumes at 20 cents. 38 sales (72 percent) are at 16 cents or below, while a little more than half the volume is sold at 16 cents or below. . . . Arithmetically the large volumes at 20 cents would have a strong effect on the weighted average of 15.16 cents per Mcf, but these should be discounted. . . .

The producers, on the other hand, argue that the 20 cent sales, if not given full weight, should be given some weight. The Commission adopted this consideration in *Sun Oil Co.* . . . A ceiling at 16 cents for the pre-Policy Statement period, in effect, gives some weight to the prices above 16 cents as well as the contract prices and the prices under temporary certificate, for if we gave no consideration to the prices above 16 cents, the ceiling would be set at a lower level, since ordinarily we do not set the ceiling price at the highest level.

As for the post-Policy Statement period, it may be observed that there are nine sales and moderate volumes at 15 cents, three sales and moderate volumes at 16.2 cents, one sale and a small volume at 16.5 cents, and three large sales at 18.0 cents. As the producers argue, the fact that the 18-cent prices were established in abridged hearings should not detract from their weight in setting the line. . . .

We are of the opinion that 17.0 cents per Mcf . . . is the in-line price for the period following September 28, 1960. It is our judgment that this conclusion gives appropriate weight to the comparatively large volumes sold under permanent certificates at 18.0 cents per Mcf while reflecting the weighted average price of 16.17 cents per Mcf. In addition, a 17.0 cent price clearly gives some weight to the unconditioned contract prices and to the prices under temporary certificates. Finally, some 43 percent of the gas has been permanently certificated at a price higher than 17.0 cents. One proposed sale . . . is at 17.0 cents, under a contract dated October 1, 1963. Giving due consideration to all sales in the area during the period in question, an in-line price of 17.0 cents is fully justified. H.A. 284-286.

In *Sinclair* the trial examiner determined the pre-Policy Statement in-line price as follows:

Applying the criteria for the determination of an in-line price, as developed by the numerous Commission and Court decisions following Catco, to the data in the foregoing tabulation, resulted in a numerically weighted average price of 16.68 cents per Mcf and a

volumetrically weighted average price of 17.18 cents per Mcf. In according the proper evidentiary weight to the evidence of record, most reliance or the greatest weight has been accorded the 14 permanently certificated sales with an estimated first months' delivery volume of 460,575 Mcf. These sales and volumes do not "reflect current conditions in the industry" because of their limited nature. Having accorded the greatest weight to the permanently certificated sales and in giving appropriate consideration to temporary certificated sales at substantial volumes presently moving in interstate commerce, it is concluded the public convenience and necessity requires the natural gas here under consideration at an in-line price of 16.0 cents per Mcf at 14.65 psia.

The in-lineness of the 16.0 cents per Mcf here determined may be further demonstrated. The Commission said in *Texaco-Seaboard Inc., et al.,* 27 FPC 482, 485, and *Hassie Hunt Trust (Operator) et al.,* 30 FPC 1438, 1445, ". . . as brought out in *Catco* and . . . in Texaco-Seaboard, the price line does not accord with the highest price or prices permanently authorized but falls between the highest group of prices and the median price." Applying this test to Staff Chart 3, Exhibit 4, [the price array] . . . , reveals a median price of 14.57 cents (volumetric weighted average) which, when averaged with the highest price of 17.59 cents, produces an in-line price of 16.08 cents per Mcf.

A similar test further illustrates the in-lineness of the 16.0 price per Mcf.

Using *all* permanently (77) and *all* temporarily (35) certificated sales related to *all* volumes of natural gas (4,390,500 Mcf) moving in interstate commerce during the period after September 28, 1960, and through March 10, 1964, from District No. 2, a volumetrically weighted average price of 15.15 cents per Mcf is indicated. This median price when averaged with the highest temporarily certificated price of 18.00 cents per Mcf produces an in-line price of 16.57 cents per Mcf. S.A. 181-82.

Of the post-Policy Statement in-line price, the examiner said:

For the 22 sales being made in the 14.0 to 14.75 cent price level in the above tabulation [the price array],

> the numerically weighted average price is 14.25 cents and the volumetrically weighted average price is 14.35 cents per Mcf at 14.65 psia. However, the numerically weighted average price for the 29 sales is 14.58 cents per Mcf and the volumetrically weighted average price is 14.84 cents per Mcf at 14.65 psia. Considering the foregoing data and the evidence of record showing the history of prices and the price patterns in District No. 2, the Examiner is of the opinion that the present or future public convenience and necessity requires the natural gas here under consideration at an in-line price of 15.0 cents per Mcf at 14.65 psia. S.A. 185-86.

The Commission further explained the method of selecting the post-Policy Statement in-line price as follows:

> A totaling of all permanently and temporarily certificated sales in District No. 2 under contracts dated after September 28, 1960 and through March 10, 1964, exclusive of the sales to Valley at 14 cents, shows a listing of 101 sales involving a combined estimated first month volume of 4,060,388 Mcf. The median price on a volumetric basis is 16.00 cents and the volumetric weighted average price is 15.29 cents. Approximately 53 percent of the estimated first month volume covered by these sales moved in the price range of from 16 cents to 18 cents. On the basis of these calculations, and with recognition of the fact that the temporarily certificated sales represented most of the sales above the 16 cents price level, and should not be accorded undue weight, and giving some weight to the unconditioned contracts we conclude that the price of 16 cents per Mcf represents the correct post-policy in-line price of jurisdictional sales of natural gas in District No. 2. In reaching this result we may observe that if we confined ourselves to permanently certificated sales we would not find a line as high as 16 cents, for the next highest sales are at the 15.25 cents level. S.A. 225-26.

UNITED STATES COURT OF APPEALS

TENTH CIRCUIT

Nos. 7912, 7962, 8115, 8116, 8118,
8119, 8121, 8122, 8123, 8124, 8125

JANUARY TERM, 1967

PAN AMERICAN PETROLEUM CORPORATION; E. COCKRELL, JR.; CONTINENTAL OIL COMPANY; FREEPORT SULPHUR COMPANY; GENERAL AMERICAN OIL COMPANY OF TEXAS; J. RAY McDERMOTT & CO., INC.; PLACID OIL COMPANY, *et al.*; SHELL OIL COMPANY; THE SUPERIOR OIL COMPANY; and U.S. OIL OF LOUISIANA INC.,

Petitioners,

v.

FEDERAL POWER COMMISSION,

Respondent.

LONG ISLAND LIGHTING COMPANY; PHILADELPHIA ELECTRIC COMPANY; PHILADELPHIA GAS WORKS DIVISION OF THE UNITED GAS IMPROVEMENT COMPANY; PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,

Intervenors.

ON PETITIONS TO REVIEW ORDERS OF THE FEDERAL POWER COMMISSION

HAROLD H. YOUNG, JR. for the petitioner in Nos. 7912 and 7962; NEAL POWERS, JR. for the petitioners in Nos. 8115, 8118 and 8125; JOSEPH C. JOHNSON for the petitioner in No. 8116; CECIL E. MUNN for the petitioner in No. 8119; PAUL W. HICKS for the petitioners in No. 8122; OLIVER L. STONE for the petitioner in No. 8123; and HERBERT W.

Varner for the petitioner in No. 8124. With them on the briefs were:

J. P. Hammond, William P. Hardeman, Carroll L. Gilliam, Phillip R. Ehrenkranz, and Grove, Jaskiewicz, Gilliam & Putbrese for Pan American Petroleum Corporation, petitioner in Nos. 7912 and 7962;

Cecil N. Cook and Butler, Binion, Rice, Cook & Knapp for E. Cockrell, Jr., petitioner in No. 8115, Freeport Sulphur Company, petitioner in No. 8118, and U.S. Oil of Louisiana Inc., petitioner in No. 8125;

Bruce R. Merrill and Thomas H. Burton, Jr., for Continental Oil Company, petitioner in No. 8116;

W. P. Barnes, Jere G. Hayes, and Cantey, Hanger, Gooch, Cravens & Scarborough for General American Oil Company of Texas, petitioner in No. 8119;

H. H. Hillyer, Jr. and H. H. Hillyer, III for J. Ray McDermott, Inc., petitioner in No. 8121;

Robert W. Henderson for Placid Oil Company, Margaret Hunt Hill, Trustee for Hassie Hunt Trust, H. L. Hunt and Hunt Oil Company, petitioners in No. 8122;

Thomas G. Johnson for Shell Oil Company, petitioner in No. 8123;

Murray Christian for The Superior Oil Company, petitioner in No. 8124.

Howard E. Wahrenbrock for the respondent. With him on the brief were Richard A. Solomon, General Counsel, Cyril S. Wofsy, Attorney, and Joel Yohalem, Attorney, Federal Power Commission.

Before Lewis, Breitenstein and Hill, Circuit Judges.

Lewis, Circuit Judge.

These petitions by independent natural gas producers seek review under section 19(b) of the Natural Gas Act [1] of orders entered by the Federal Power Commission establishing an "in-line" price and other conditions for permanent certificates of public convenience and necessity issued under section 7 of the Act and covering sales of gas in interstate commerce from producing areas in South Louisiana and the adjacent federal domain offshore.[2] Proceedings before the Commission encompassed some 362 separate certificate applications, two-thirds of which were settled and severed before the conclusion of hearings, for a wide variety of gas-sales contracts executed between 1945 and 1963.[3] By its orders the Commission set the "in-line" price, or maximum initial price, at 18.5 cents per Mcf, with an additional 1.5 cents per Mcf for tax reimbursement where the gas is produced within the taxing jurisdiction of Louisiana. Refunds were required, with interest, for amounts in excess of the in-line price previously collected under temporary certificates that contained express provisions for potential refund liability. All permanent certificates that issued were made subject to a moratorium on increased-rate filings above 23.55 cents per Mcf, including tax reimbursement, pending completion of the South Louisiana area rate proceeding or July 1, 1967, whichever is earlier. Finally, for those producers whose temporary certificates contained no refund conditions, the Commission reserved for further consideration the question of whether they would in fact be required to make refunds.

The petitions are before this court by virtue of the fact that Pan American Petroleum Corporation, petitioner in Nos. 7912 and 7962, has its principal place of business within the territorial bounds of this circuit and was the

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[1] 15 U.S.C. § 717r(b).

[2] Union Texas Petroleum *et al.*, Opinions Nos. 436 and 436-A, reported at 32 F.P.C. 254 and 32 F.P.C. 952.

[3] The petitions for review by four producers have been separately considered in this court. See Continental Oil Co. v. FPC, — F2 —, Feb. 10, 1967.

first producer to file for review. The other petitioners are transfers from other circuits. 28 U.S.C. § 2112(a). The four intervenors are parties of record, but upon their election not to file briefs we denied their requests to present oral arguments.

At the hearings below, several producers offered economic and geological evidence which purported to reflect an increase in production costs from those that had prevailed during prior South Louisiana certificate proceedings. The examiner rejected this evidence, the Commission sustained the examiner, and some of the petitioners here have filed motions to adduce. Action on the motions was deferred until completion of arguments on the merits of the orders. We have since held in Sunray DX Oil Co. v. FPC, — F2 —, Dec. 9, 1966,[4] that the standards of public convenience and necessity to be applied by the Commission in section 7 proceedings do not compel admission of such evidence. And while circumstances surrounding certificate applications may on occasion dictate consideration of cost factors, these are matters subject in the first instance to Commission expertise and discretion. *United Gas Improvement* v. *Callery Properties, Inc.*, 382 U.S. 223, 227. Here, as will be discussed, the Commission's orders are based partially upon comparisons between current prices and in-line prices previously established. Concededly, current economic and geological cost evidence could have a substantial effect upon final disposition of the applications. But for purposes of section 7, there is nothing in the record to suggest an abuse of Commission discretion in the rejection of such evidence, and accordingly, the motions to adduce will be denied. We turn then to the substantive content of the orders and the producers' various objections thereto.

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[4] References hereinafter to *Sunray DX* will be to the Dec. 9, 1966 decision of this court, — F2 —, unless otherwise noted.

The In-Line Price

The origin of the in-line price concept is the landmark *CATCO* decision, Atlantic Ref. Co. v. Public Service Comm'n of New York, 360 U.S. 378, where the Supreme Court admonished the Commission to hold the line on natural gas prices pending determination of just and reasonable rates. Since *CATCO*, numerous court opinions have attempted to articulate and refine the evidentiary standards and methodology for in-line pricing. See, *e.g.*, United Gas Improvement Co. v. Callery Properties, Inc., 382 U.S. 223; Sunray DX Oil Co. v. FPC, 10 Cir., — F2 —, Dec. 9, 1966; California Oil Co., Western Div. v. FPC, 10 Cir., 315 F2 652; Public Service Comm'n of New York v. FPC, D.C. Cir., 329 F2 242, *cert. denied sub nom.*; Prado Oil & Gas Co. v. FPC, 377 U.S. 963; United Gas Improvement Co. v. FPC, 9 Cir., 283 F2 817, *cert. denied sub nom.*; Superior Oil Co. v. United Gas Improvement Co., 365 U.S. 879. From these and other authorities, two principles have emerged which more than once have presented the Commission with delicate problems of reconciliation. The first is that the price line must reflect current conditions in the industry and the prices on which the line is based must be those under which substantial quantities of gas presently move in interstate commerce. The second is that the Commission must be suspect of all current prices that are under review in pending court or Commission proceedings or that were arrived at by methods which subsequently have been disapproved in unrelated proceedings.

It was almost impossible for the Commission to adhere fully to both of these principles in the instant proceedings. Because of the substantial number of temporary certificates involved and the recent history of South Louisiana in-line price litigation, the majority of interstate gas volume from the area was moving under suspect prices. In a sense, current conditions in South Louisiana had to be treated as

suspect. Under the circumstances, therefore, the Commission looked to the 18.5-cent price line (exclusive of tax reimbursement) that had been established in three previous South Louisiana cases,[5] and adopted the view that, absent sufficient evidence showing the contrary, the old line would be presumed to have continued. All of the three previous decisions involved sales under contracts executed in the period 1956-1959. Absent the severed dockets, the instant case involves sales under contracts executed in the period 1957-1963.

One of the important factors that the Commission had to consider was whether the amendments to its Statement of General Policy No. 61-1, 24 F.P.C. 818, might have caused a general increase in permanently certificated prices for the South Louisiana area. The Statement established twenty-three geographic rate areas and proposed guideline prices for each area. When originally issued in September 1960, it did not set guidelines for South Louisiana because of pending litigation. On October 25, 1960, however, the Commission issued its First Amendment to the Statement, 24 F.P.C. 902, which fixed the South Louisiana guideline price at 21.5 cents per Mcf exclusive of tax reimbursement. Then on October 31, 1961, the Commission issued its Fourth Amendment to the Statement, 26 F.P.C. 661, which lowered the South Louisiana guideline price to 21.25 cents per Mcf, including tax reimbursement, and set a guideline of 19.5 cents per Mcf for gas produced in the adjacent federal domain offshore. In light of these amendments,

[5] These were: United Gas Pipeline Co., 30 F.P.C. 329, *dismissed for lack of venue sub nom.* Gulf Oil Corp. v. FPC, 5 Cir., 330 F2 824; Placid Oil Co., 30 F.P.C. 283, *aff'd sub nom.* United Gas Improvement Co. v. Callery Properties, Inc., 382 U.S. 223, *reversing* 5 Cir., 335 F2 1004; and Continental Oil Co., 27 F.P.C. 96 (*CATCO* on remand). None of these cases involved consolidation of dockets on a scale as great as the instant one.

the Commission tabulated all recent permanently certificated prices [6] according to four contract periods, *viz*:

(1) Prior to January 1, 1960, which was covered by the maximum price line (18.5 cents plus 1.5 cents for tax reimbursement where applicable) established in the three previous South Louisiana in-line cases (see note 5 *supra*);

(2) From January 1, 1960 to October 25, 1960, the date of the First Amendment to Statement of General Policy No. 61-1;

(3) From October 26, 1960 to October 31, 1961, the date of the Fourth Amendment to Statement of General Policy No. 61-1; and

(4) From November 1, 1961 to the end of 1962. The Commission then compared the weighted average permanent-certificate prices with the respective weighted average temporary-certificate prices in each contract period. The only temporary certificates considered were those involved in the instant proceeding. The findings and conclusions of the Commission may be summarized as follows:

For the calendar years in the first contract period, the weighted average price, including tax reimbursement, varied from 20.8814 cents to 21.8988 cents under permanent certificates and from 19.5573 cents to 22.2080 cents under applicable temporary certificates. Since these figures corresponded closely with the evidence on which the three prior in-line determinations were based, the Commission concluded that there was no reason to depart from the line that those cases had established.

For the second contract period, the weighted average price, including tax reimbursement, was 21.767 cents under permanent certificates and 22.76 cents under applicable temporary certificates. It was also found, however, that

[6] Apparently all other price sources, including settlement agreements, were deemed suspect. The examiner characterized settlement agreements as being of "doubtful validity," but there was no elaboration on this point.

almost two-thirds of the permanently certificated volume for the period moved at 23.25 cents, a figure that was approved when the Commission was applying pricing standards in certificate cases which have since been disapproved by the courts. But rather than ignore altogether this unusually high price, the Commission simply observed that the weighted average price for permanently certificated sales was within the limits of the pre-1960 weighted average prices and concluded that the price line had not changed.[7]

For contracts falling in the period between issuance of the two guideline prices, the weighted average price, including tax reimbursement, was 17.148 cents under permanent certificates and 21.25 cents under applicable temporary certificates. Here, however, temporary volumes outweighed permanent volumes by almost four to one. For contracts dated after issuance of the second guideline price, or the fourth period, the weighted average price, including tax reimbursement, was 15.0194 cents under permanent certificates and 20.87 cents under temporary certificates. But here temporary volumes outweighed permanent volumes by more than nine to one and, in addition, the weighted average price for permanent certificates was quite distorted by an extremely low-priced sale at 10.75 cents. In view of the relatively few permanently certificated sales in these last two periods and the distortion caused by the one substantial low-priced sale, the Commission concluded that the marked decline in weighted average prices from those of the first two periods did not warrant a reduction of the previously established in-line price. Accordingly, the Commission ordered that for sales subject to the taxing jurisdiction of Louisiana, the price line would be held at 18.5 cents plus 1.5 cents for tax reimbursement.

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[7] If we ignore the sales at 23.25 cents, as the Commission could have done under the suspect-price doctrine, the weighted average price under permanent certificates for the second contract period would be 19.32 cents, including tax reimbursement.

No permanent certificates and only eight temporary certificates were issued for sales from the adjacent federal domain during the three periods subsequent to January 1, 1960. The weighted average prices under the temporary certificates were 21.5 cents for the second period and 19.5 cents for the third and fourth periods. The Commission concluded that these few sales were insufficient to show a change in the previous 18.5-cent price line for that offshore area.

Petitioners' threshold argument is that the findings and conclusions of the Commission are not supported by substantial evidence. To the contrary, we think the record shows commendable diligence in the presentation to the parties and to the court of the analytical approach, computation methods, and relevant data which led to the results reached. We further think that the conclusions relating to the 18.5-cent price line based upon the record findings are clearly reasonable.

Petitioners suggest that the price line has been subjectively pre-determined by reference to the three previous South Louisiana cases, and since some of the petitioners were not parties to those other proceedings, it is contended that they have been denied procedural due process. While such an argument has merit when considered in the abstract, it here does no more than beg the question. The Commission was careful to explain that although the previously established in-line price would be presumed to continue, it would be used simply as a point of departure in analyzing the more recent price evidence. In the end, it was demonstrated that, if anything, prices had declined rather than increased since the determination of the earlier price lines. The determination made here cannot be held invalid just because it is premised in part upon a comparison of current prices with earlier prices.

Petitioners next urge that the Commission erred in failing to give greater weight to the relatively large volumes of gas moving at prices in excess of 18.5 cents. In effect,

they accuse the Commission of having applied the suspect-price doctrine in such a manner that it became mathematically impossible not to freeze the results to old price lines that had no current relevancy. We note that in Placid Oil Co., 30 F.P.C. 283, *aff'd sub nom. United Gas Improvement Co.* v. *Callery Properties, Inc.*, 382 U.S. 223, *reversing* 5 Cir., 335 F2 1004, the Commission eliminated all sales in excess of 18.5 cents even though such sales, both numerically and volumetrically, represented well over half of the interstate total. The Supreme Court held that the 18.5-cent line was supported by the record. Here, in contrast to the *Callery* case, all permanently certificated sales, those above 18.5 cents as well as those below, were reflected in the Commission's computations. And although some of the computations were distorted by two permanent certificates at 23.25 cents and one permanent certificate at 10.75 cents, it is clear that neither the high-priced nor the low-priced sales were ignored or eliminated from consideration.

Petitioners also complain about the use of weighted averages to arrive at ceiling prices. Naturally, average prices are lower than the highest prices paid. As a matter of mathematical simplicity, however, there is nothing wrong with using weighted averages to compare one set of numbers with another. As we stated in the *Sunray DX* case, *supra*, a comparison of weighted average prices is proper so long as it is not arbitrary and capricious. We find nothing arbitrary or capricious about the procedure followed here. In *Sunray DX* the Commission concluded that the in-line price should be raised while here it concluded that it should remain unchanged. But different results cannot condemn the method used.

Petitioners' final contention aimed at the in-line price issue is that the guideline prices established by the First and Fourth Amendments to Statement of General Policy No. 61-1 should be presumed to represent in-line prices from the points of view of producers. Our position on this

question has already been set out in the *Sunray DX* opinion and a full restatement of that position here is unnecessary. Whatever reliance producers might have placed on the guideline prices, that reliance cannot be traced to any misleading statements by the Commission. Guideline prices are, and were here, issued *ex parte,* without opportunity for a hearing as required by section 7, and not subject to judicial review. *Wisconsin* v. *FPC,* D.C. Cir., 292 F2 753. It cannot be seriously contended that they represented equivalents to the in-line prices required by *CATCO* for the issuance of permanent certificates of public convenience and necessity. *Public Service Comm'n of New York* v. *FPC,* D.C. Cir., 329 F2 242, *cert. denied sub nom. Prado Oil & Gas Co.* v. *FPC,* 377 U.S. 963. We reiterate that having once established guideline prices the Commission could not totally ignore their effect on the in-line price. But here, as in *Sunray DX,* their effect was thoroughly evaluated.

In summation, we find that the Commission has approached the instant case with full appreciation for its importance to the producers as well as to the consumer. Aside from the deference we owe Commission expertise, *California* v. *FPC,* 9 Cir. 353 F2 16, 23, we are satisfied that the record evidence amply supports all of the substantive conclusions pertaining to the in-line price of 18.5 cents. We reach this conclusion, as we have indicated, in reliance upon the soundness of our earlier decision in *Sunray DX.* The District of Columbia Circuit has had recent occasion to refuse acceptance of some aspects of our reasoning in *Sunray DX,* although tacitly recognizing, as did we, that evidentiary standards must of necessity not be so inflexible as to frustrate the already-complex administration of the Natural Gas Act. *Public Service Comm'n of New York* v. *FPC,* D.C. Cir., F2 , Feb. 7, 1967. We do not believe that the simple purpose of a section 7 proceeding is to protect the consumer against exploitation pending determination of a just and reason-

able rate. But see *Public Service Comm'n of New York* v. *FPC, supra* at slip op. pp. 24-25. The general purpose of the Act is to protect the consumer, but section 7 proceedings, as well as other proceedings in the administration of the Act, must consider and attempt to obtain a balance between the interests of consumer, producer and all others whose interests fall between. The task is difficult, but experience has gradually attached more than lip-service significance to administrative expertise. Temporary certificates are now conditioned rather than perfunctorily granted. Contract prices have made some adjustment in view of the inescapable captured market of regulation. The establishment of guidelines is a considered administrative function. Settlement agreements are a recognized and judicially encouraged instrument to provide both a semblance of price stability to producers and to mitigate against delay to the consumer interests. See generally *Continental Oil Co.* v. *FPC*, 10 Cir., F2 , Feb. 10, 1967; *Skelly Oil Co.* v. *FPC*, 10 Cir., F2 (*Permian Basin*), Jan. 20, 1967. We consider each of these procedural and background incidents to have proper evidentiary significance in a section 7 proceeding to be weighed by the Commission against the impact of more probative evidence such as permanent certificates in its determination of in-line prices. The rejection of economic and geological evidence, although not necessarily unrelated to current conditions, may be required for practical reasons. See *United Gas Improvement Co.* v. *Callery Properties, Inc.*, 382 U.S. 223.

Tax Reimbursement

Although we affirm the Commission's conclusions that the previously established 18.5-cent price line had not changed over the four contract periods, we find no support for the rather summary treatment of the 1.5-cent additional allowance for tax reimbursement where the gas is sold subject to the taxing jurisdiction of Louisiana. In *United Gas Improvement Co.* v. *FPC*, 9 Cir., 283 F2 817, 826,

cert. denied sub nom. Superior Oil Co. v. *United Gas Improvement Co.,* 365 U.S. 881, it was held:

> "[C]omparative tax reimbursement plans as well as comparative base rates ought to be taken into consideration in determining whether a proposed initial price is out of line. Except where the difference in tax reimbursement features is relatively insubstantial, it is our opinion that failure to take account of such a difference would be an abuse of discretion."

During most of the contract period covered by the three prior South Louisiana in-line cases, the State of Louisiana imposed a severance tax on natural gas production of 1.5 cents per Mcf. In August 1958, an additional "gathering" tax of one cent was added, but its collection was suspended on November 30 of the same year when the tax was challenged as unconstitutional.[8] In lieu thereof, on December 1, 1958, the severance tax was simply increased by one cent to 2.5 cents per Mcf. See generally Pan American Petroleum Corp v. FPC, D.C. Cir., 322 F2 999. The reimbursement in the three prior cases was of course 1.5 cents, reflecting the full amount of the state severance tax being collected on the dates of most of the applicable contracts. The same tax reimbursement was given in the instant case without even acknowledging that there had been a change in the tax itself. Under the Ninth Circuit's *U.G.I.* decision, such action, unsupported by either evidence or logic, would indicate an abuse of discretion.[9]

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[8] It was ultimately held unconstitutional by the Supreme Court of Louisiana in Bel Oil Corp. v. Fontenot, 238 La. 1002, 117 So.2 571.

[9] In the brief and on oral argument, counsel for the Commission stated that the Supreme Court's *Callery* decision had disposed of the problem adversely to the producers. The *Callery* opinion, however, does not mention the propriety of the tax reimbursement, probably because the issue was not even before the Court when the case was originally submitted. The producers briefed the tax-reimbursement problem, along with several other issues, for the first time in their petition for rehearing. The petition was denied without opinion. 382 U.S. 1001.

Not knowing what the tax reimbursement might otherwise be, we are not in a position to determine whether the difference would be "relatively insubstantial." Petitioners have supplied the court with copies of an exhibit showing contract provisions for natural gas sales in South Louisiana from 1954 to 1962. They also refer to other evidence which, they contend, dictates a tax allowance of "at least 1.99¢ and in no event less than 1.8¢ per Mcf." From the collective points of view of the producers in the area, the differences could prove to be quite substantial. These portions of the record, however, have not been certified to us and included in the Joint Appendix, and in any event, it is the Commission that must first address itself to the problem.

The price conditions ordered by the examiner were:

> "(1) 18.5 cents per Mcf if the certificate relates to a sale not subject to the taxing jurisdiction of Louisiana, and (2) 20 cents per Mcf if the certificate relates to a sale subject to Louisiana tax."

And those ordered by the Commission were:

> "18.5 cents per Mcf at 15.025 psia, plus reimbursement for Louisiana severance tax, where applicable, of not more than 1.5 cents per Mcf."

Whether the Commission misconstrued the examiner's decision or was purposely emphasizing that the in-line price had not changed from that previously established, the difference between the methods of treatment is important. Both conclusions were based upon comparative contract prices which included tax reimbursement. The examiner ordered a 20-cent price *in*cluding tax reimbursement while the Commission ordered an 18.5-cent price *ex*cluding tax reimbursement. Obviously, if the unreimbursed severance tax paid by the producers is greater than 1.5 cents, their revenue will be below the Commission determined base price of 18.5 cents. We find nothing in the record or in the arguments of counsel to justify a reduction of the tax reimbursement allowance below contract amounts. It appears that the pre-1958 contract allowances have been sum-

marily imposed on petitioners, and all history of changes in taxes and contract provisions have been ignored. We therefore remand this issue to the Commission for further consideration.

The Moratorium

Some of the petitioners object to the imposition of a moratorium on new rate filings in excess of 23.55 cents, including tax reimbursement, until final determination of the South Louisiana area rate or July 1, 1967, whichever is earlier. They contend that this condition in their permanent certificates has no support in the record to show that it is required by public convenience and necessity. This same contention was made about an identical moratorium provision in the *Callery* case, *United Gas Improvement Co.* v. *Callery Properties, Inc.*, 382 U.S. 223. The Supreme Court there held:

> "We think, contrary to the Court of Appeals, that there was ample power under § 7(e) for the Commission to attach these conditions for consumer protection during this interim period . . .
>
> "The 'in-line' price of 18.5 cents is supported by the contract prices in the south Louisiana area that were not 'suspect,' and the selection of 23.55 cents beyond which a price increase might trigger escalation reflects the Commission's *expertise.*" 382 U.S. at 228-29. (Emphasis by the Court.)

See also *FPC* v. *Texaco, Inc.*, 377 U.S. 33, 42-43; *FPC* v. *Hunt*, 376 U.S. 515. The rationale of these authorities is equally applicable to the conditioning of certificates by Commission-approved take-or-pay provisions, provisions which require no separate consideration at this time. We therefore approve the Commission action on this aspect of the case.

Interest on Refunds

The Commission's orders require payment of refunds of amounts previously collected in excess of the in-line price [10] where temporary certificates were issued subject

to such refund liability. The orders require further that interest be paid at six percent per annum on excess amounts collected before March 1, 1960 and at seven percent per annum on excess amounts collected thereafter.[11] Those petitioners whose temporary certificates did not mention interest on refunds contend that there is neither an equitable basis nor legal authority for this portion of the orders. They insist that interest may commence running only from the date that their refund obligations became liquidated, and then only at a rate which is deemed compensatory. *Rodgers* v. *United States,* 332 U.S. 371; *Billings* v. *United States,* 232 U.S. 261. These arguments, however, ignore the prior case law as it specifically relates to FPC proceedings. In *Texaco, Inc.* v. *FPC,* 5 Cir., 290 F2 149, 157, and *Mississippi River Fuel Corp.* v. *FPC,* D.C. Cir., 281 F2 919, 927, *cert. denied* 365 U.S. 827, the courts approved orders imposing six percent interest on refunds even though the sellers had no express notice that interest might be required. And in *Callery, supra,* where a seven percent rate was imposed without notice, the Supreme Court stated simply that "the imposition of interest on refunds is not an inappropriate means of preventing unjust enrichment." 382 U.S. at 230.[12] Here, too, we approve the action taken by the Commission.

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[10] Or in excess of the price floor fixed in certain temporary certificates if the floor is higher than the in-line price.

[11] March 1, 1960 is the date of issuance of Order No. 215A, 23 F.P.C. 474, where interest payable on refunds as increased from six to seven percent.

[12] Petitioners suggest that they are being discriminated against because in five other recent opinions the Commission set the rate at only 4½ percent. The Commission explains that all of those cases involved situations where, once the amount to be refunded became liquidated, the producers were given the option of holding the fund or depositing it in an escrow account where it would be invested in short-term government obligations, both pending an order of distribution.

REFUNDS UNDER UNCONDITIONED TEMPORARY CERTIFICATES

As in our *Sunray DX* case, petitioners vigorously object to the portion of the Commission's orders that defers for further consideration the questions of whether and to what extent refunds will be required where temporary certificates were issued without express refund conditions. And while, unlike *Sunray DX*, we are not aware of any recent Commission action directing petitioners with unconditioned temporary certificates to make refunds out of the subject sales, we are nevertheless convinced that there is sufficient aggrievement for review at this time. On the authority of the *Skelly* case, *Public Service Comm'n of New York* v. *FPC*, D.C. Cir., 329 F2 242, *cert. denied sub nom. Prado Oil & Gas Co.* v. *FPC*, 377 U.S. 963, the Commission has ruled that it has "both the power and the duty to require refunds of amounts collected in excess of the 'in-line' price" even where temporary authorizations are silent as to potential refund liability. Skelly Oil Co., *et al.*, Opinion No. 492, June 1, 1966.[13] Many producers, in reliance upon prior assurances that all of the moneys collected under such authorizations was theirs to keep,[14] have spent

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[13] See also Sun Oil Co., *et al.*, Opinion No. 502, July 28, 1966; Amerada Petroleum Corp., *et al.*, Opinion No. 501, July 27, 1966; Turnbull & Zoch Drilling Co., *et al.*, Opinion No. 499, July 25, 1966; H. L. Hawkins, *et al.*, Opinion No. 498, July 22, 1966.

[14] See FPC Chairman Swidler's published address to the 1961 annual meeting of the American Petroleum Institute. See also 29 F.P.C. 223, 225, where in denying intervenors' motions to impose refund conditions on previously issued unconditioned temporary certificates, a unanimous Commission stated:

> "[W]e would be in a position of having induced producers to dedicate their gas to the market upon one set of conditions, and then imposing more stringent conditions upon them. Such a course of action, except under the most extraordinary conditions, would appear to be inconsistent with the Commission's obligation to act upon applications with 'such certainty as to allow the exercise of choice upon (the producer's) part'. *Sunray Mid-Continent Oil Company* v. *F.P.C.*, 270 F2 404. Equally important it would so denature the value of a Commission authorization as to place any reliance upon our actions in this area in serious jeopardy."

or reinvested the proceeds from their sales and would be hard put to find now the substantial amounts necessary for refunds. Inasmuch as the Commission's position on the merits of the issue is firmly established, albeit in opinions not related to this case, the threat of loss to these petitioners is real and imminent, and judicial consideration of their liability need not be postponed. *Columbia Broadcasting System, Inc.* v. *United States,* 316 U.S. 407, 417-21; *Sunray DX Oil Co.* v. *FPC,* 10 Cir., 351 F2 395, 400; *Hinton* v. *Udall,* D.C. Cir., 364 F2 676, 680.

We held in *Sunray DX* that "refunds may be ordered under § 7 only when a producer contractually undertakes to make such refunds by the acceptance of a temporary certificate containing an express refund condition."[15] We adhere to that decision for purposes of this case and see no reason for duplication here of principles and views already discussed. We shall, however, consider one contention that has been made by the Commission and not covered in the *Sunray DX* opinion. It is that every producer selling gas under an unconditioned temporary certificate should be charged with notice that refunds might be ordered as of the date of the District of Columbia Circuit's *Skelly* decision. From then on, says the Commission, "a producer should have taken steps to protect himself in the event refunds were ordered, and if he failed to do so, he has no equity to plead which will affect his refund obligation."[16] Aside from the fact that the *Skelly* decision could directly affect only the parties involved, we think that at that time producers generally still had every reason to believe that such refunds would not be ordered. The decision said that the Commission has the power to order refunds even though temporary certifi-

[15] — F2 at —. The rule would not apply of course where an unconditioned temporary certificate has not become final and is overturned by a reviewing court. United Gas Improvement Co. v. Callery Properties, Inc., 382 U.S. 223, 229.

[16] H. L. Hawkins, *et al.*, Opinion No. 498, p. 3, July 22, 1966.

cates do not warn of this contingency, that exercise of this power is not necessarily mandatory, but that when the power is not exercised the record must show the equitable considerations involved. When petition for certiorari was filed by producers a very short time after the decision, the Commission filed a brief in opposition stating that "it is entirely possible . . . that the Commission, after reviewing all pertinent factors, will again reach the conclusion that refunds are inappropriate." It is difficult to imagine how a case in this posture could have dictated immediate preparation for a turning away from years of Commission assurances [17] and from what was believed to be settled judicial interpretation.[18]

Both the Commission and the courts have repeatedly acknowledged that stability of prices is one of the great objectives of regulation under the Natural Gas Act. We have been especially mindful of this objective in our consideration of the moratoria on new rate filings and other restrictive conditions in the producers' licenses to sell gas in interstate commerce. It is manifest, however, that price stability is undermined by threats or attempts to fix prices retroactively without prior warning or, even worse, with prior assurances that specifically negate the refund contingency. Such action not only violates fundamental notions of due process, it also defeats a fundamental purpose for which the regulation was created. The Commission has stated that "temporary authorizations are not and could never be a vehicle for assuring such [price] stability by the very method by which they are handled." Skelly Oil Co., *et al.*, Opinion 492, p. 4, June 1, 1966. We emphatically disagree. The very fact that many temporary authorizations now contain refund conditions attests to their role in holding the line against changing prices. And whatever the method by which temporary authorizations are handled, we

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[17] See note 14 *supra*.

[18] Sunray Mid-Continent Oil Co. v. FPC, 10 Cir., 270 F2 404, 408-10; *cf.* FPC v. Hope Natural Gas Co., 320 U.S. 591, 618.

consider it unconscionable to impose upon an unwary producer a hidden liability which could very well, had it been originally exposed, have influenced the initial producer decision of whether to dedicate his gas to interstate commerce. The principle of imposing and enforcing a retroactive condition where none exists, if carried to the extreme, could expand to render a fully established section 5 just and reasonable rate totally unstable and always subject to the lurking possibility of refund. The harm is only more apparent in the latter case.

The motions to adduce additional evidence are denied. All cases are remanded to the Commission for further proceedings consistent with this opinion.